

competitive market, both EchoStar and DIRECTV will have a strong incentive to deliver what consumers want most.<sup>61</sup>

**b. EchoStar's Promise To Provide Local Service Is Unenforceable.**

30. Commenting on New EchoStar's recent announcement that it plans to carry all local broadcast channels, Bob Scherman, the editor of a leading trade publication covering the satellite industry, observed that this proposal is "a very shrewd political Hail Mary, with no downside because it is unenforceable."<sup>62</sup> NRTC believes this analysis is correct.

31. First, the Applicants' promise to carry all stations in all markets is not a binding legal obligation. EchoStar has historically shown a willingness to skirt even legal obligations relating to carriage of local stations, so this empty promise should be given no credit.<sup>63</sup>

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<sup>61</sup> In an attempt to discredit NRTC's current views regarding the feasibility of local-into-local service, the Applicants highlight statements made by NRTC two years ago during the Commission's SHVIA proceeding. *See Opposition*, p. 16. NRTC readily admits that its view regarding carriage of local stations has evolved over the past few years along with developments in law, technology and the marketplace. With the passage of the SHVIA, the provision of local broadcast channels in local markets has become extremely popular. For example, the Satellite Broadcasting and Communications Association (SBCA) found that in 13 markets where local-into-local service was introduced via DBS, there was a 43% increase in subscribers. *See SBCA Comments, In re Annual Assessment of the Status of Competition in the Market for the Delivery of Video Programming*, CS Docket No. 00-132, p. 8 (filed July 2000). On several occasions, the Commission has concluded that the significant recent increase in DBS subscribership can be attributed to the authority in the SHVIA for DBS carriers to retransmit local broadcast signals. *See Seventh Annual Report, In the Matter of Annual Assessment of the Status of Competition in the Market for the Delivery of Video Programming*, 22 CR 1414, FCC 01-1, ¶13 (*Seventh Video Competition Report*). *See also Eighth Annual Report, In the Matter of Annual Assessment of the Status of Competition in the Market for the Delivery of Video Programming*, FCC 01-389, ¶8 (*Eighth Video Competition Report*). In fact, DIRECTV informed the Commission that its overall subscriber levels increased by 20 percent due to the provision of local television service. *Eighth Video Competition Report*, ¶59. Since NRTC filed its Comments in July 2000, the Applicants also have demonstrated the economic viability of serving local broadcast markets through the launch -- or planned launch -- of four additional spot-beam satellites (DIRECTV 4S and EchoStar VII were launched on November 27, 2001 and November 21, 2002, respectively; while EchoStar VIII and DIRECTV 7S are pending launch dates). Finally, as discussed by Walter Morgan, compression ratios for DBS satellites are now 12:1 and will likely increase over time as technologies further develop and additional capacity becomes available for the retransmission of local signals. *See Declaration of Walter Morgan*, p. 23 (Exhibit O to the *NRTC Petition*).

<sup>62</sup> Gregory MacDonald, "Opinion: Broadcasters Oppose Satellite-Dish Merger," *Helena Independent Record*, March 17, 2002.

<sup>63</sup> *See e.g. Petition to Deny or Conditionally Grant of Paxson Communications, Inc., In the Matter of EchoStar Communications Corporation, General Motors Corporation and Hughes Electronics Corporation*, CS Docket No. 01-348, pp. 6-9 (filed February 4, 2002).

32. Indeed, only ten days after representing to the FCC that it would comply with SHVIA and carry all stations in all markets on a single dish, EchoStar beat a hasty retreat.<sup>64</sup> On March 7, 2002, in a brief filed with the U.S. Supreme Court seeking to overturn SHVIA, EchoStar stated that “the merged entity does not intend to carry all channels in every market unless the decision below [upholding the constitutionality of the carry one, carry all provision of SHVIA] is upheld.”<sup>65</sup>

33. On March 15, 2002, in response to an effort by the NAB to point out the hypocrisy of EchoStar’s position, EchoStar confirmed the company’s unwillingness to carry all local stations in all markets, stating that:

If must carry is upheld, we will obviously fully comply with the law. If must carry is overturned, we fully intend to carry all local stations *with meaningful local content* in all 210 local broadcast markets.<sup>66</sup>

This response shows, once again, that EchoStar’s bold public statements are rendered far less meaningful after careful review of the details, qualifications and nuances. Stripped of its rhetoric, New EchoStar plans to selectively carry only those stations that broadcast the type of content New EchoStar unilaterally deems meaningful. Since consumers in rural markets will no longer have a choice in providers, they will be required to accept New EchoStar’s sole judgment about the “meaningfulness” of local content to be made available to them.

34. Second, it is unclear when New EchoStar actually would carry local stations in all markets. It offers only to provide such service “. . . as soon as 24 months” after approval.<sup>67</sup> This

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<sup>64</sup> *Opposition*, p. 4. See also *Judiciary Testimony*.

<sup>65</sup> *SBCA Petition*, n. 2.

<sup>66</sup> Letter from Karen Watson of EchoStar, to U.S. Senators, dated March 15, 2002 (emphasis added).

<sup>67</sup> *Opposition*, p. 4.

open-ended promise means rural Americans may never receive local service from the monopoly created by this Merger. Given its track record of hiding devils in details, it is not difficult to anticipate pleas of “changed circumstances” and other excuses to justify the failure to live up to this vague promise.<sup>68</sup>

35. Absent competition, the only way to ensure that local service is extended to all Americans is to establish an extensive and costly regulatory scheme to strictly enforce the Applicants’ promise. Yet, time and time again, the FCC has recognized that competition is far preferable to regulation.<sup>69</sup>

36. As NRTC and others have demonstrated, the provision of local service has been driven by competitive reactions of one Applicant to the other. It is for this reason that the Applicants each serve substantially the same markets.<sup>70</sup> The temptation to sacrifice this functioning competitive market for a regulated monopoly should be avoided.<sup>71</sup> As the Commission is well aware, innovations that benefit consumers, such as the provision of local television service in all markets to all Americans, are best driven by competition.

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<sup>68</sup> EchoStar also leads the FCC to believe that it will provide these local services with “one consumer friendly mini-dish,” *Opposition*, p. 4, yet it urges the FCC to “. . . reject attempts to impose a special condition on the combined company that it carry all its must carry stations so they are received on the same dish.” *Id.*, p. 140.

<sup>69</sup> See Memorandum Opinion and Order, *In the Matter of Applications for Consent to Transfer of Control of Licenses and Section 214 Authorizations from Tele-Communications, Inc., Transferor to AT&T Corp., Transferee*, 14 FCC Rcd 3160, ¶14 (1999); *AOL Time Warner Order*, ¶15. See also “Connecting the Globe: A Regulator’s Guide to Building a Global Information Community,” Press Statement of Chairman William E. Kennard on “Wireless Day.” See also Press Conference of Chairman Michael K. Powell, “Digital Broadband Migration,” October 23, 2001. Similarly, Commissioner Kevin Martin also spoke to the need for greater facilities-based competition, saying: “I believe the government – particularly the Commission – should place a higher priority on facilities-based deployment and competition. The goal of the Telecommunications Act was to establish a competitive and deregulated environment. But to get to true deregulation, we need facilities-based competition.” Remarks of Commissioner Kevin J. Martin at the National Summit on Broadband Deployment, October 26, 2001.

<sup>70</sup> *NRTC Petition*, Exhibit M: DMAs Served by DIRECTV and EchoStar.

<sup>71</sup> There are also public safety benefits in having multiple facilities-based competitors providing services via satellite.

## **2. Broadband Deployment Will Suffer If The Merger Is Approved.**

37. If there is one thing on which both the Applicants and NRTC agree, it is that rural Americans are underserved by broadband. How this digital divide is best bridged, however, remains a point of sharp contention. In their *Application*, the Applicants argue that only the proposed Merger will permit broadband services to evolve in rural America. NRTC and others have shown, however, that the Merger is not necessary to promote broadband deployment in rural areas. EchoStar and Hughes each can provide broadband service to a “critical mass” of subscribers. Further, the Merger would effectively discourage new entrants from providing competing services.

### **a. Broadband Competition Should Not Be Sacrificed In Rural America.**

38. The Applicants argue that “the merger of EchoStar and Hughes will *create* for the first time a truly competitive broadband alternative to DSL and cable modem service.”<sup>72</sup> However, competition among DSL, cable modem and satellite services exists only in areas of the country where such services are available. In rural America, satellite is often the only broadband technology available.

39. The Applicants complain that their Ku-band service offerings are subject to constraints on transmission speeds, capacity and overall cost.<sup>73</sup> While this may or may not be true, the Merger is not the right vehicle to correct these purported shortcomings. Rather, improvements on transmission speeds are best accomplished through the competitive forces that drive innovations in technology.<sup>74</sup> The capacity constraints they complain about are nothing

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<sup>72</sup> *Opposition*, p. 80 (emphasis in original).

<sup>73</sup> *See Opposition*, p. 90.

<sup>74</sup> *See In the Matter of Inquiry Concerning the Deployment of Advanced Telecommunications Capability to all Americans in a Reasonable and Timely Fashion, and Possible Steps to Accelerate Such Deployment Pursuant to*

more than a function of the choices that EchoStar and Hughes have made, for example, to use certain capacity for pay-per-view programming rather than for broadband; they could certainly make more Ku-band spectrum available for broadband services if they chose to do so, particularly in unserved rural areas.<sup>75</sup>

40. Regarding the Ka-band, as NRTC observed in its Petition, New EchoStar would have a total of six full-CONUS slots, providing it with market power in the rural broadband market that would effectively bar any additional entry.<sup>76</sup> The Applicants, relying on selective “simple arithmetic,”<sup>77</sup> note that there would be eleven other entities with full-CONUS coverage ability. They fail to acknowledge that no single remaining entity would have more than two slots. With three times as many slots, at least twice as much spectrum as their “competitors,” and the ability to bundle video and other services, New EchoStar’s simple arithmetic is nothing more than fuzzy math.<sup>78</sup> Clearly, EchoStar and DIRECTV individually stand a far greater chance of success in providing Ka-band broadband service than any other single Ka-band licensee.

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*Section 706 of the Telecommunications Act of 1996*, FCC 99-5, CC Docket No. 98-146, 14 F.C.C.R. 2398, ¶1 (1999) (“One of the fundamental goals of the Telecommunications Act of 1996 (the 1996 Act) is to promote innovation and investment by multiple market participants in order to stimulate competition for all services, including broadband, communications services.”).

<sup>75</sup> The Applicants misinterpret NRTC’s evidence showing that ILECs charge monopoly prices where they do not face competition. *See Opposition*, p. 95. The point of this argument is that the combined New EchoStar would, as a rural broadband monopoly, follow the same path of increasing prices, as there would be no competitor to constrain prices in such areas.

<sup>76</sup> *NRTC Petition*, p. 46.

<sup>77</sup> *Opposition*, pp. 109-110.

<sup>78</sup> NRTC did not state, as the Applicants incorrectly claim, that SPACEWAY has access to three full-CONUS slots and EchoStar has access to five full-CONUS slots. To set the record straight, NRTC stated that Hughes and PanAmSat together controlled three full-CONUS slots and EchoStar controlled three full-CONUS slots. *See NRTC Petition*, p. 46.

**b. The Merger Would Give New EchoStar Unrivalled Satellite Broadband Market Power.**

41. The Applicants' claims about the competitiveness of other broadband distribution systems are without merit:

- The public announcements of Sprint, WorldCom and Nucentrix to scale back and delay conversion of MMDS systems to two-way data distribution suggest that it could be several years before MMDS spectrum is deployed for two-way fixed wireless service, if ever.<sup>79</sup>
- That three Ka-band licensees recently notified the FCC that they had commenced construction of their satellite systems hardly means competition is imminent. The milestone does not in any way suggest that actual construction has begun, and certainly cannot be construed to mean that a satellite will actually be placed in operation.<sup>80</sup>
- Assuming the truth of the statistics the Applicants cite concerning unlicensed terrestrial use, service to parts or all of 503 counties -- out of a total of 3,141 counties -- hardly constitutes significant competition. Such unlicensed operations do not enjoy interference protection from other systems or even household devices using 802.11b and related technologies. The range of these systems, relative to satellite, is also extremely restricted.

For these reasons, the extent to which these technologies are likely to become viable competitors is entirely speculative. Potential technologies that may be developed in the future are, for purposes of this Merger review, entirely beyond the scope of this proceeding.<sup>81</sup>

42. For rural America, New EchoStar would enjoy a broadband monopoly. Despite the Applicants' claims that the existing StarBand and DIRECWAY Ku-band services are inferior,

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<sup>79</sup> The Applicants address this fact only with irrelevant statistics on the expected coverage area and analysts' projections on potential commercial viability. *Opposition*, pp. 111-112.

<sup>80</sup> In order to meet the "commence construction" milestone, Ka-band licensees need only enter into a "non-contingent" satellite construction contract. See Order and Authorization, *Application of VisionStar, Incorporated, Licensee, Shant Hovnanian, Transferor And Echostar Visionstar Corporation, Transferee*; 24 CR 1326, ¶22 (2001). See also *Norris Satellite Communications, Inc.*, 12 FCC Rcd 22299, ¶9 (1997); *AMSC Subsidiary Corp.*, 8 FCC Rcd 4040, ¶14, n. 27 (1993).

<sup>81</sup> In addition to the possible development of MMDS and other satellite broadband systems, the Applicants cite the prospect of new DSL standards. Such speculation about future technologies cannot be properly injected into a public interest, competition analysis. See *infra* ¶57.

this argument has marginal appeal only with respect to the ability of EchoStar and Hughes to compete against DSL and cable modem services in areas where those services are available. It has nothing to do with the situation in rural America, where StarBand and DIRECWAY are often the only alternatives and where the prices of those services are much higher than in those local markets where DSL and cable modem services compete.<sup>82</sup>

**3. The Applicants Have Failed To Demonstrate That The Alleged Efficiencies Are Merger Specific.**

43. According to the Commission, claimed efficiencies "must be merger specific, and therefore, efficiencies that could be achieved through means less harmful to the public interest than the proposed merger cannot be considered true benefits of the merger."<sup>83</sup> As the Commission recently held, "[e]fficiencies that are vague, speculative, and unverifiable will not be considered in evaluating the competitive effects of the proposed transaction."<sup>84</sup> The *Merger Guidelines* also make clear that the Applicants are required to demonstrate that the efficiencies it claims are merger specific.<sup>85</sup>

44. The Applicants' alleged efficiencies are not specific to the proposed Merger. For instance, NRTC and others demonstrated in their Petitions that there are several means by which EchoStar and DIRECTV each could deliver all local broadcast channels to all markets.<sup>86</sup> This

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<sup>82</sup> NRTC Petition, pp. 50-51.

<sup>83</sup> GTE-Bell Atlantic Order, ¶240.

<sup>84</sup> See *In the Matter of the Application of Air Virginia, Inc. (Assignor) and Clear Channel Radio Licensee, Inc. (Assignee) For Consent to the Assignment of the License of WUMX (FM), Charlottesville, VA*, MM Docket No. 02-38, FCC 02-53, ¶30 (*Air Virginia*).

<sup>85</sup> *Merger Guidelines* at § 4.

<sup>86</sup> NRTC Petition, pp. 63-65; NAB Petition, pp. 89-91.

could be accomplished through a joint venture between the parties or with a third party. It also could be accomplished separately, through more efficient use of existing spectrum.<sup>87</sup>

45. The Applicants "anticipate" that the Merger will facilitate the standardization of functionally superior equipment.<sup>88</sup> But they fail to explain how this anticipated efficiency is a benefit, or how it is remotely related to the Merger. In fact, equipment can be standardized without resorting to a merger to monopoly.

46. The Applicants' prediction that their increased subscriber base will decrease programming costs which "may be" the basis for new programming is also not an efficiency created by the Merger. Rather, it is the exercise of market power by a monopolist able to leverage its dominance in distribution to advantage itself in negotiations with program suppliers.

47. In the *Air Virginia* case, the Commission recently designated for hearing a broadcast application that would result in two entities controlling more than 94 percent of the Charlottesville, Virginia radio advertising market.<sup>89</sup> The applicants claimed various efficiencies and benefits that would lower advertising rates and increase format choices. This evidence was disputed by a petitioner that contended that advertising rates had not been proven to be lower and that the format changes would result in less diversity. The Commission held that there was not enough information in the record to show that the efficiencies would be realized and thus designated the assignment application for hearing.

48. NRTC does not believe that a hearing is necessary in the proposed Merger, for two reasons. First, unlike *Air Virginia*, this case involves a merger to monopoly. Second, there are

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<sup>87</sup> NRTC Petition, pp. 57-69; Pegasus Petition, pp. 38-44.

<sup>88</sup> Opposition, p. 26.

<sup>89</sup> *Air Virginia*, ¶8.



no material facts at issue. It is clear from the pleadings that the claimed efficiencies are, on their face, illusory, non-existent or unrelated to the Merger. Assuming that it is even appropriate to consider efficiencies in a merger to monopoly, given EchoStar's failure to meet its burden of proof in establishing the nexus between the claimed efficiencies and the Merger, there is an insufficient basis to conclude that the benefits of this Merger outweigh the obvious competitive harm.

**D. The Anti-Competitive Effects Of The Merger Are Indisputable.**

49. The Applicants have not shown -- nor can they -- that the proposed Merger will enhance competition.<sup>90</sup> To the contrary, the Merger would have severe anti-competitive effects. Following the Merger, tens of millions of consumers will have no choice in MVPD provider. The head-to-head competition between EchoStar and DIRECTV, which has benefited all consumers, would be eliminated.

**1. Other Technologies Are Not Comparable To DBS.**

50. To address the obvious loss of consumer choice resulting from the proposed Merger, the Applicants argue that MMDS, SMATV and C-band are reasonable substitutes for DBS in areas not served by cable. Recent Commission reports, however, show that these technologies have suffered from dramatic losses in subscribership and are available, if at all, in only small pockets of the country.<sup>91</sup>

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<sup>90</sup> As Commissioner Copps recently stated in the context of the *Air Virginia* case, "For a robust marketplace of ideas to survive, *each community* must have a diversity of sources of information available to its members -- not just a *variety* of formats, but *diversity* of formats and of ownership. See *Air Virginia*, Statement of Commissioner Copps. Obviously, the instant Merger, with 100% ownership concentration for the delivery of MVPD programming throughout vast portions of the country, raises far more serious concerns regarding media concentration than a 94.2% consolidation between two entities in a single, small radio market.

<sup>91</sup> See *NRTC Petition*, pp. 23-28.

51. The notion, for instance, that MMDS operators will be able to bundle MVPD and broadband services across the allocated spectrum ignores realities related to the unavailability of equipment, the need to address inter-system interference and the rights of educators and commercial licensees as lessors of the spectrum.<sup>92</sup> More fundamentally, no MMDS operator has announced plans to provide bundled services using the MMDS spectrum.

52. Similarly, the Applicants cannot truly believe that C-band is competitive with DBS in rural America. Subscribership continues to decline dramatically and there are no indications that consumers are willing to continue purchasing large dish antennas.<sup>93</sup>

53. The Applicants' claim that New EchoStar will be subject to effective competition from C-band, MMDS and SMATV also directly contravenes EchoStar's previous statements in its lawsuit against DIRECTV. In that proceeding, EchoStar clearly admitted in response to Requests for Admissions that it did not compete with C-band; it did not compete with MMDS; and it did not compete with SMATV.<sup>94</sup>

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<sup>92</sup> While arguing that the "competitiveness of MMDS video offerings will likely be enhanced" by their roll-out of broadband services, *Opposition*, p. 52, the Applicants ignore that the FCC itself already has concluded that "most MMDS licenses will not be used in the future to compete in the MVPD market." *NRTC Petition*, p. 26, citing *Seventh Video Competition Report*, ¶88. Furthermore, DIRECTV itself recently removed any doubt as the viability of MMDS to provide MVPD services: within the last week or so, Nucentrix, a leading MMDS provider, entered into agreements with DIRECTV and Pegasus to convert the majority of its pay-TV subscriber base to satellite. Under the new agreements with DIRECTV and Pegasus, Nucentrix will promote DIRECTV as a replacement for its MMDS services. *Wireless Cable Op Sending Subs to DBS*, SKYREPORT, March 21, 2002.

<sup>93</sup> See *Seventh Video Competition Report*, ¶83; See also *Eighth Video Competition Report*, ¶67 (the number of subscribers abandoning the C-band service increased from 840 per day to more than 1,300 per day between the *Seventh Video Competition Report* and the *Eighth Video Competition Report*). The Applicants find it "odd" that as "one of the four major distributors of C-band programming," NRTC characterized C-band as a "fringe technology." There is nothing odd about it. Along with the rest of the C-band industry, NRTC's C-band subscribership has dropped dramatically in recent years and is currently less than 20,000. With this limited subscriber base, the Applicants inexplicably characterize NRTC as a "major" distributor of C-band service. *Opposition*, p. 51.

<sup>94</sup> Reply In Support Of DIRECTV's And Hughes' Motion To Determine Sufficiency Of Plaintiff's Response To Request For Admission No. 2, Civil Action No. 00-K-212 (U.S.D.C., Dist. of Colorado), Nov. 30, 2000. See also Plaintiffs' Response to DIRECTV's and Hughes' First Set of Requests For Admissions, Civil Action No. 00-K-212 (U.S.D.C., Dist. of Colorado), Sept. 8, 2000.

54. Regarding future competition from NRTC, the Applicants argue that "...NRTC's *exclusive* rights are limited and will expire in the future."<sup>95</sup> From this, they conclude (without explanation) that "[a]s a consequence, New EchoStar will be able to compete fully with NRTC/Pegasus throughout those areas where NRTC and Pegasus have distribution rights under their contracts."<sup>96</sup> To say the least, it is unclear how the expiration of NRTC's exclusive distribution rights will somehow allow NRTC and Pegasus to "compete fully" with New EchoStar. As explained in detail in the *NRTC Petition*, following the Merger NRTC would not be positioned to compete effectively with New EchoStar under any circumstances.<sup>97</sup>

55. The Applicants repeated assertion that NRTC "overcharges" rural consumers by \$3.00 a month is wrong.<sup>98</sup> NRTC's members are free to price their services at the local level. However, they typically follow DIRECTV's recommended national price. They do not, as a matter of course, increase the recommended national price by \$3.00 as the Applicants claim, although some members and Pegasus may not follow DIRECTV's recommendations in all cases.<sup>99</sup>

56. Even more specious -- and hypocritical -- is the Applicants' argument that future technologies not yet developed or deployed will offer competition to the merged entity. On one hand, the Applicants quote the *Merger Guidelines* for the proposition that "proper competition analysis is limited to alternatives that are 'practical in the business situation faced by the merging

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<sup>95</sup> *Opposition*, p. 51 (emphasis in original).

<sup>96</sup> *Id.*

<sup>97</sup> *NRTC Petition*, pp. 28-30.

<sup>98</sup> See e.g., *Opposition*, p. v.

<sup>99</sup> Pegasus is an affiliate, not a member, of NRTC.

firms' and should not rely on alternatives that are 'merely theoretical.'"<sup>100</sup> Then, in discussing competitive MVPD alternatives, the Applicants point to competition that may emerge from foreign DBS satellites,<sup>101</sup> MVDDS<sup>102</sup> and electric utilities.<sup>103</sup> None of these technologies, under any stretch of the imagination, is poised to offer significant competition to New EchoStar.

57. The Applicants cannot have it both ways. The *Merger Guidelines* were deliberately drafted to prevent consideration of possible competitors that may never enter the market, especially where, as here, there are substantial barriers created by the very high fixed costs required to enter the market.

## **2. The Number Of Households Unpassed By Cable Is Much Larger Than The Applicants Claim.**

58. While clinging to their discredited story that 97.1% of all television households in the United States have access to cable -- a figure that defies reality<sup>104</sup> -- the Applicants also assert that the number of homes passed by cable is merely a "red herring."<sup>105</sup> They claim that the number is not "decisionally significant," because New EchoStar will be unable to isolate such homes for

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<sup>100</sup> *Opposition*, p. 8.

<sup>101</sup> No foreign DBS satellite currently serves the U.S. market, and future service from foreign slots is theoretical at best. Also hollow is the Applicants' claim that "other companies have ample opportunity to use satellite spectrum and orbital locations ... in an attempt to introduce additional competition in the MVPD market," and their related claim that "ample FSS spectrum remains available for medium-power and high-power satellite DTH initiatives." *Opposition*, pp. 49, 50.

<sup>102</sup> The MVDDS applications cited by the Applicants as yet another competitor to DBS, are not even granted by the Commission, let alone operational or feasible in rural America. See *NRTC Petition*, pp. 23, 27-28.

<sup>103</sup> The electric and gas utilities that the Applicants claim "appear to hold great promise for competition in rural areas" are undefined. *Opposition*, p.53. There are no specifics provided by the Applicants as to the identity of these theoretical competitors, the scope or nature of their services, or how their terrestrially-based business plans would somehow hold "great promise" or make commercial sense for rural America.

<sup>104</sup> See *NRTC Petition*, pp. 6-16, for a discussion of how New EchoStar has relied on flawed data to create the false impression that cable services are available throughout virtually the entire country.

<sup>105</sup> *Opposition*, p. 66.

anticompetitive pricing and behavior.<sup>106</sup> In any event, they respond that “national pricing” will protect from discrimination any homes not passed by cable.<sup>107</sup>

59. Contrary to the Applicants’ claims, the number of homes not passed by cable is critically important to the Commission’s evaluation of the proposed Merger. It represents the universe of homes located in different markets throughout the country that currently rely solely on EchoStar and DIRECTV to receive MVPD services.

60. The Applicants take exception to NRTC’s reliance on data and observations by the National Telecommunications and Information Administration (NTIA) and the Rural Utilities Service (RUS). They argue that the availability of cable to unoccupied housing units and occupied households without a television is “indisputably irrelevant.”<sup>108</sup> As NTIA and RUS pointed out, however, the cable industry’s methodology for calculating the percentage of Homes Passed *includes* unoccupied housing units and occupied households without television sets -- and thereby creates an artificially high number of Homes Passed.<sup>109</sup> If homes are counted as passed by cable regardless of whether they are occupied, and regardless of whether they have a television set, then the resulting number should be divided into *all Housing Units* (which include

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<sup>106</sup> *Id.*

<sup>107</sup> *Id.*, pp. 60, 65-66. Indeed, price discrimination is not the only problem created by a monopoly. In all households not passed by cable, consumers will have no choice in MVPD provider. They will be required to take service on the terms and conditions established by New EchoStar, or they will have to do without MVPD service altogether.

<sup>108</sup> *Opposition*, p. 60.

<sup>109</sup> This conclusion was not “entirely unsupported,” as the Applicants erroneously claim. *Opposition*, p. 61. In addition to pointing out obvious deficiencies in the cable industry’s methodology described above, NRTC attached to its Petition a copy of the actual Questionnaire sent to cable operators by Kagan. *NRTC Petition*, p. 10; Exhibit E. It makes abundantly clear that cable operators are not asked to -- and do not -- count only occupied housing units and “TV Households” in determining the number of homes passed by their systems. While the Applicants claim that cable operators have “every incentive to determine [the correct homes passed] figure because it defines their potential local customer base,” in fact they have every incentive to *inflate* this number for that very reason (*e.g.*, increased advertising revenues). *Opposition*, p. 61.

all homes, regardless of whether they are occupied or have television sets), not TV Households (which include only occupied Housing Units with television sets).

61. It is this false and misleading number -- 97.1% -- that the Applicants point to as proof that few homes ("only" 3,000,000<sup>110</sup>) will be left without an MVPD alternative if the Merger is approved. When calculated correctly, however, as NTIA and RUS show, the percentage of Homes Passed is closer to 81% (leaving 23,000,000 households without access to cable).<sup>111</sup> This disparity clearly is *not* "indisputably irrelevant," as the Applicants' claim.<sup>112</sup> It shows the devastatingly harmful impact of the proposed Merger on consumers located in specific markets across the country where there is no access to a cable alternative.<sup>113</sup>

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<sup>110</sup> DIRECTV's own internal surveys show that *more than three million households are not passed by cable just among DIRECTV's own 10.7 million subscribers. DIRECTV 2001 Cable Comments*, p. 13 (stating that only 71% of DIRECTV customers live in areas able to receive cable television service). If extrapolated nationwide, as pointed out in the *NRTC Petition*, DIRECTV's own surveys lead to the conclusion that some 35,000,000 homes may not be passed by cable. See *NRTC Petition*, p. 15. See also *NAB Petition*, p. 47; *Pegasus Petition*, pp. 17-18. New EchoStar's assertion that the 3,000,000 figure may actually be *too high* is an astonishing piece of advocacy. In six states, cable operators report more Homes Passed than the Census Bureau even reports as Households. *NRTC Petition*, pp. 11-12. New EchoStar's claim that a cable pass rate of *more than 100%* is somehow unduly conservative does not warrant further response. *Opposition*, pp. 61-62.

<sup>111</sup> If homes are counted as passed by cable regardless of whether they are occupied, and regardless of whether they have a television set, then the resulting number should be divided into *all Housing Units* (which include all homes, regardless of whether they are occupied or have television sets), not TV Households (which include only occupied Housing Units with television sets). By performing the math correctly, the percentage of Homes Passed by cable *decreases* from 97% to 81%, while the number of homes *not* passed by cable *increases* from approximately 3,000,000 to 25,000,000. See *NRTC Petition*, pp. 5-16. See also National Telecommunications and Information Administration and Rural Utilities Service, *Advanced Telecommunications In Rural America: The Challenge of Bringing Broadband Service to All Americans*, April, 2000, n. 62.

<sup>112</sup> The Applicants attempt to quibble with NRTC's reliance in some instances on Warren data and in others on Kagan data. *Opposition*, p. 62-63. First, as well recognized by the Commission, Warren data is historically *more conservative* than Kagan data in regard to the number of Homes Passed by cable. *Seventh Video Competition Report*, ¶18, fn. 23. NRTC's demonstration that Warren data is defective in some cases, therefore, certainly undercuts the more optimistic Kagan data. Secondly, any dispute between the merits of Warren vs. Kagan data is completely unrelated to the deficiencies in the cable industry's *methodology* of calculating the number of Homes Passed. Likewise, the Applicants' complaint that NRTC compared Kagan data unfavorably to U.S. Census Bureau data should be quickly discounted by the Commission. *Id.* The FCC may comfortably rely upon the U.S. Census Bureau for data relative to occupied households in the U.S.

<sup>113</sup> Dr. Willig compounds the error in his selection of data regarding houses unpassed by cable by assuming the existence of a national cable market in which all cable companies can be aggregated into a single cable "market share." If it is assumed that a national market exists, then all cable companies are treated as if they are one. In his own publication on mergers, Dr. Willig opines that where products are relatively homogeneous, as with cable and

62. More importantly, while the Applicants dispute the number of homes not passed by cable at the *national* level, they fail to provide any information at all regarding the dearth of competition resulting from the Merger *at the local level* -- which has always been the focus of the Commission's competitive analysis.<sup>114</sup> Instead, they attack Dr. MacAvoy's detailed and methodical assessment of post-Merger competition at the local level. But in doing so, they misapply the data used by Dr. MacAvoy.

63. The Applicants argue that some homes in areas targeted by Dr. MacAvoy as "not passed by cable" are in fact "passed by cable."<sup>115</sup> To support their attack, the Applicant analyzed DIRECTV churn data to determine whether any customers who lived in *zip codes* relied upon by Dr. MacAvoy had churned from DIRECTV to cable.<sup>116</sup> Further, the Applicants' consultant conducted a survey (the parameters of which are undefined) by contacting residents in particular

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DBS, the HHI should be calculated based on market shares reflecting capacity, not sales. In the context of the proposed Merger, this means that HHI should be calculated based on coverage, not subscribership. This approach to calculating market shares leads to the conclusion that the proposed Merger changes this national market from one in which there are three competitors with equal coverage (cable, EchoStar and DIRECTV) to one in which there are only two, New EchoStar and cable. The HHI for such a market increases from approximately 3267 to 5000, for an increase of 1733. To the extent that homes are *unpassed* by cable in this hypothetical national market, then the DBS companies, with their ability to serve *all* households, actually have a larger nationwide market share than cable and the presumed harmful effects of the Merger are further exacerbated. See Robert D. Willig, "Merger Analysis, Industrial Organization Theory, and Merger Guidelines," Brookings Papers: Microeconomics, 1991, pp. 281, 285.

<sup>114</sup> As discussed in detail in the *NRTC Petition* -- and ignored by the Applicants in their *Opposition* -- in evaluating DBS spectrum aggregation cases, the Commission has always emphasized that the relevant consideration is the state of MVPD competition at the *local* level. In approving some mergers, the Commission looked at the national Homes Passed rate and relied on the safety net created at the local level by the existence of two competing DBS providers in all areas not passed by cable. With the proposed Merger of the only two DBS providers, however, that policy rationale disappears along with the safety net. See *NRTC Petition*, pp. 16-20. See also Order and Authorization, *MCI Telecommunications Corporation, Assignor and EchoStar 110 Corporation, Assignee*, 15 CR 1038, ¶10 (1999); Order and Authorization, *United States Broadcasting Co. Transferor and DIRECTV Enterprises, Inc. Transferee*, 15 CR 645, ¶13 (1999); Order And Authorization, *Tempo Satellite, Inc., Assignor and DIRECTV Enterprises, Inc., Assignee; Application for Consent to Assign Authorization to Construct, Launch and Operate a Direct Broadcast Satellite System Using 11 Frequencies at the 119° W.L. Orbital Location*, 16 CR 27, ¶11 (1999).

<sup>115</sup> *Opposition*, pp. 63-65

<sup>116</sup> *Id.*, p. 64.

*zip codes*. Apparently, some respondents answered that cable was available. From this secret survey, the Applicants conclude that Dr. MacAvoy's analysis is defective.<sup>117</sup>

64. As described in the MacAvoy Response, however, Dr. MacAvoy did not examine zip codes in conducting his analysis of the impact of the proposed Merger at the local level. Rather, he based his analysis strictly on Census Blocks, which are far more localized. On average, there are more than 190 Census Blocks contained in a single zip code.<sup>118</sup> As a result, the Applicants' churn data and informal survey results prove nothing more than that the individuals churning from DIRECTV or contacted by DIRECTV's consultant apparently were located in those areas of the zip codes where cable was available -- but were outside the Census Blocks relied on by Dr. MacAvoy.<sup>119</sup> Dr. Willig's critique of Dr. MacAvoy's findings is premised on his misunderstanding of Dr. MacAvoy's methodology.

**3. The Applicants Ignore That The DBS Industry Is Thriving And That EchoStar And DIRECTV Are Competing Successfully Against Each Other.**

65. The Applicants paint a bleak picture of their ability to compete against cable absent the proposed Merger.<sup>120</sup> They are notably silent, however, as to their tremendous successes as independent companies -- *without* the Merger.

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<sup>117</sup> *Id.*

<sup>118</sup> As of 1999, there were 42,193 Zip Codes in the United States compared to 8 million Census Blocks identified for Census 2000, creating a ratio of approximately 190 Census Blocks per zip code. See *U.S. Census Bureau, 1999 Zip Codes* (visited March 26, 2002) <<http://www.census.gov/geo/www/tiger/zip1999.html>> (containing a data file of 42,193 zip codes); See also *Glossary* (visited March 26, 2002) <[http://www.census.gov/dmd/www/glossary/glossary\\_c.html](http://www.census.gov/dmd/www/glossary/glossary_c.html)>.

<sup>119</sup> See *MacAvoy Response*, pp. 10-11. Notably, Dr. Willig has not provided the full results of his survey. There may, in fact, be deep flaws in the analysis, or the summary information he did provide may be misleading. As one obvious example, the Applicants have not disclosed how many of those persons contacted live in areas where cable is *not* available. Presumably, the survey results will be made available for review pursuant to the Commission's Information Request dated February 4, 2002. See Letter from W. Kenneth Ferree, Chief, Cable Services Bureau, to Pantelis Michalopoulos, Counsel for EchoStar Communications, and Gary M. Epstein, Counsel for General Motors Corporation and Hughes Electronics Corporation (February 4, 2002).

<sup>120</sup> See, e.g., *Opposition*, pp. 38, 47.



66. The DBS industry, represented collectively by EchoStar and DIRECTV, is flourishing as a competitive force. More than two out of every three new MVPD subscribers choose DBS over cable.<sup>121</sup> Every day, DBS gains more than 8,500 subscribers.<sup>122</sup> In 2001 alone, EchoStar and DIRECTV reported a combined 24% increase in subscribership and a 37.5% increase in revenues totaling \$12.1 billion.<sup>123</sup> Today, there are more DBS subscribers (17.5 million) than digital cable subscribers (14.4 million).<sup>124</sup>

67. The Applicants claim -- with a straight corporate face -- that these glowing statistics create a deceptively “false, rosy” picture about the state of DBS competition.<sup>125</sup> However, their recent public statements and Earnings Reports confirm their phenomenal success as stand-alone companies competing with each other and with cable.<sup>126</sup>

68. For example, at the same time the Applicants were warning the Commission that their customers were poised to “abandon the DBS platform” if the Merger is not approved, EchoStar advised investors that it had acquired 400,000 net new subscribers in the last quarter of 2001, for a total of 1,570,000 net new subscribers for 2001 alone.<sup>127</sup> EchoStar pointed out to investors that it intends to add at least 1,170,000 net new subscribers in calendar year 2002, finishing the year

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<sup>121</sup> The DBS industry’s current subscriber growth rate is nearly two and a half times cable’s. *Eighth Video Competition Report*, ¶8.

<sup>122</sup> *Id.*, ¶58.

<sup>123</sup> See *NRTC Response*, p. 4; *National Rural Electric Cooperative Association Comments*, submitted February 4, 2002, pp. 5-6; *Petition to Deny of the Communications Workers of America*, submitted February 4, 2002, pp. 3-4; *Petition to Deny of the American Cable Association*, submitted February 4, 2002, p. 12; *Pegasus Petition*, p. 9. See also *Eighth Video Competition Report*, ¶57, Appendix C, Table C-1.

<sup>124</sup> See *Kagan Broadband*, February 28, 2002, p. 1.

<sup>125</sup> *Opposition*, pp. 66-67.

<sup>126</sup> See *EchoStar Investment Call*; See also *Hughes Investment Call*. See also “*EchoStar Ends 2001 On Positive Note*,” *Satellite Business News*, March 13, 2002, p.1.

<sup>127</sup> *EchoStar Investment Call* (statement of Michael McDonnell, Chief Financial Officer, EchoStar.).

with more than 8,000,000 subscribers. These subscriber additions, as noted by EchoStar, will reflect a growth rate in the “high teens.”<sup>128</sup>

69. Similarly, in January 2002, Hughes reported a 13% increase in subscribers and stated that it expected to add 1,200,000 net new subscribers during calendar year 2002, including 200,000 to 250,000 during the first quarter.<sup>129</sup> This accomplishment, in their words, will constitute a “stellar year.”<sup>130</sup> Even so, on March 21, 2002, Hughes raised its first quarter guidance. Based on quarter-to-date performance, DIRECTV increased its subscriber projections by 62.5%, to 325,000 net new subscribers for the first quarter alone.<sup>131</sup>

70. The Applicants’ revenue numbers are even more extraordinary. While cautioning the Commission about their “degraded ability to compete with cable” absent the proposed Merger, EchoStar reported a 47% increase in revenues over the previous year, and projected revenues for 2002 to be 20 to 25% *higher*.<sup>132</sup> Not to be outdone, Hughes reported the “largest quarterly revenues in [its] history,” noting that the increase was due primarily to the “continued strong demand for DIRECTV services in both the United States and Latin America.”<sup>133</sup>

71. Charles Ergen, EchoStar’s CEO, recently trumpeted his company’s ability to compete (notably, without the Merger):

EBITDA for the fourth quarter was 171 million, our best ever, as we continue to lever the economies of scale inherent in the DBS platform... We posted significant positive EBITDA in all four quarters in 2001, and currently

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<sup>128</sup> *EchoStar Investment Call*.

<sup>129</sup> *Hughes Investment Call*, p. 5.

<sup>130</sup> *Id.* at p. 2 (statement of Jack Shaw, President and CEO of Hughes, noting DIRECTV in the U.S. expects to have a stellar year, by bringing over a million new subscribers).

<sup>131</sup> *See Hughes Press Release*.

<sup>132</sup> *EchoStar Investment Call*.

<sup>133</sup> SEC Form 8K, filed by Hughes Electronics, Inc., January 15, 2002, p. 1.

expect 2002 EBITDA to be approximately 80 to 100% higher than 2001 EBITDA.<sup>134</sup>

72. These are not the signs of struggling or failing competitors that need to merge in order to compete successfully against the entrenched cable industry, as the Applicants would have the Commission believe. Rather, these statistics demonstrate that facilities-based DBS competition is succeeding and producing tangible public interest benefits, without the unwarranted Merger of the nation's only high power, full-CONUS DBS providers.

73. Not only is DBS thriving, but EchoStar and DIRECTV are competing vigorously, one against the other. In his original Declaration, Dr. Willig took the position that EchoStar and DIRECTV did not compete against one another.<sup>135</sup> In their Opposition, EchoStar and DIRECTV finally concede that they do compete "to an extent," but they attempt to minimize their competition by producing "churn data" showing that "only nine percent of DIRECTV's current subscribers were previously EchoStar subscribers."<sup>136</sup> They then leap to the conclusion that no substantial competition exists between the two and that their subscriber acquisition efforts are devoted almost exclusively to "luring" subscribers away from cable.<sup>137</sup>

74. On its face, the Applicants' intra-DBS churn data shows that almost 1 out of 10 DIRECTV subscribers was "taken" from EchoStar. Presumably, a similar percentage of EchoStar's subscribers was "taken" from DIRECTV. This hardly presents a compelling case that the two companies do not compete for each others' subscribers. Instead, it shows significant

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<sup>134</sup> *EchoStar Investment Call*.

<sup>135</sup> *Willig Declaration*, n. 5, n. 25.

<sup>136</sup> *Opposition*, pp. 42-43.

<sup>137</sup> *Id.*, p. 43.

intra-DBS competition -- especially considering the expense and inconvenience for existing DBS subscribers to convert to new reception systems.

75. More importantly, the Applicants' intra-DBS churn data do not address at all the competition between EchoStar and DIRECTV for other types of new subscribers (*i.e.*, those who do not happen to be current subscribers of the other DBS provider). In particular, as described in the *MacAvoy Response*, the Applicants' churn data ignore competition between EchoStar and DIRECTV for potential subscribers from the pool of existing cable subscribers. Moreover, the data ignore potential new subscribers from the pool of those who currently subscribe to *no* MVPD services, especially in rural areas where the two DBS providers are the only sources of MVPD service.<sup>138</sup>

76. NRTC and others have shown beyond doubt that competition between EchoStar and DIRECTV -- not just for the other's current subscribers, but for *any* new subscribers, including cable and non-current-DBS subscribers -- is a virtual "ping pong" match.<sup>139</sup> Repeatedly, one offers a special deal only to be followed shortly thereafter by a similar offering from the other. These consumer benefits would be eliminated if the Merger were approved.

77. The Applicants' attempt to discredit what everyone knows to be a fact is unavailing. Even DIRECTV Chairman Eddy Hartenstein recently conceded that "when we first announced the merger *we were two separate companies, competing companies in the same [market]*

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<sup>138</sup> *MacAvoy Response*, pp. 6-8. Dr. MacAvoy demonstrates, for instance, that the only two sellers of a nearly identical product have vigorously contested the acquisition of new subscribers by undertaking what EchoStar calls SAC or "subscriber acquisition costs." To initiate a larger percentage gain in new subscribers, Dr. MacAvoy shows that they offer discounts on equipment and installation that increase SAC. *Id.*, p. 8.

<sup>139</sup> *NRTC Petition*, pp. 33-34.

*space.*<sup>140</sup> Despite the Applicants' denials, there can be no doubt that EchoStar and DIRECTV are in fact vigorous competitors with one another.

78. The documented success of EchoStar and DIRECTV clearly undercuts their claim that "[a]bsent a merger, there is a profound risk that DBS will devolve from its current position in the MVPD market as a quality and innovations leader to a lesser alternative that will cause its customers to abandon the DBS platform."<sup>141</sup> Indeed, the record in this proceeding is devoid of *any* evidence to support the Applicants' claim. Their claim is a smokescreen, pure and simple. It provides no basis for the Commission to act favorably on the Merger.

## II. CONCLUSION.

EchoStar and DIRECTV have fallen far short of satisfying their burden of proving by a preponderance of the evidence that the proposed Merger would serve the public interest. The proposed Merger is clearly inconsistent with the Commission's long established goals of promoting facilities-based competition and consumer choice in the delivery of both multichannel video programming and broadband services. Approval of the Merger would result in the ultimate flip-flop -- from a thriving, facilities-based competitive marketplace to a highly regulated one controlled by a monopolist.

The *Application* should be denied.

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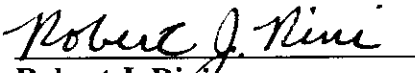
<sup>140</sup> Jeffrey Williams, "EchoStar, DirecTV Leap into Local-into-Local Politics," Satellite Business News, March 13, 2002, p. 1.


<sup>141</sup> *Opposition*, p. 38

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**April 4, 2002**



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ORIGINAL

Exhibit 1

BEFORE THE  
FEDERAL COMMUNICATIONS COMMISSION  
WASHINGTON, D.C. 20554

<i>Application of</i>	)	
	)	
EchoStar Communications Corporation,	)	
General Motors Corporation,	)	
Hughes Electronics Corporation,	)	
	)	
Transferors	)	CS Docket No. 01-348
	)	
and	)	
	)	
EchoStar Communications Corporation	)	
	)	
Transferee	)	
	)	
For Authority to Transfer Control	)	

REPLY DECLARATION OF PAUL W. MACAVOY ON BEHALF OF THE  
NATIONAL RURAL TELECOMMUNICATIONS COOPERATIVE

In Response to the Declaration of Dr. Robert D. Willig on behalf of  
EchoStar Communications Corporation, General Motors Corporation, and Hughes  
Electronics Corporation



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